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C O N F I D E N T I A L SECTION 01 OF 03 TOKYO 002110

SIPDIS

STATE PASS TO USTR FOR CUTLER, BEEMAN
TREASURY FOR IA - DOHNER, WINSHIP, POGGI
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GENEVA PASS TO USTR
NSC FOR LOI

E.O. 12958: DECL: 07/30/2018

TAGS: [ECIN](#) [ETRD](#) [EINV](#) [PREL](#) [ASEAN](#) [APEC](#) [JA](#)

SUBJECT: JAPAN'S AGENDA ON REGIONAL ECONOMIC INTEGRATION

TOKYO 00002110 001.2 OF 003

Classified By: DCM James Zumwalt for Reasons 1.4 (b,d).

¶1. (SBU) Summary: The priority of trade liberalization in the future economic architecture of Asia dominated debate among the 16 country representatives preparing the Japanese-sponsored "Track II" study on a possible ASEAN Plus 6 economic agreement. Japanese participants in the study group indicated substantial progress on trade liberalization would be difficult, even for Japan. As a result, other issues -- energy and environment, economic cooperation, and trade and investment facilitation -- enjoy equal treatment with trade liberalization in the report which will be submitted to ASEAN Economic Ministers in August. Despite acknowledgement by participants in the study of the importance of "open regionalism" in an ASEAN Plus 6 framework, the impression remains that Japan's aim is to consolidate economic relations with its Asian neighbors without opening sensitive sections such as services and agriculture or diminishing its reliance on export-led growth.
End summary.

Background

¶2. (SBU) In the spring of 2006, Japan's then Minister of Economy, Trade, and Industry Toshihiro Nikai floated a proposal for a regional economic agreement that would include the 10 ASEAN member states along with Japan, China, South Korea, Australia, New Zealand, and India. The main goal of the proposal was to present an alternative to a new regional architecture based on ASEAN Plus 3, a study for which was underway with Chinese sponsorship. Japan's proposal to establish a group of experts from the relevant countries to study the feasibility of the ASEAN Plus 6 framework -- known as the "Comprehensive Economic Partnership with East Asia"

(CEPEA) -- received the blessing of the ASEAN and other related economic ministers in August 2006, with the formal study beginning in May 2007. The study's conclusions will be presented at the August 26-29 Singapore meetings between ASEAN economic ministers and their dialogue partners.

CEPEA Debate Centers on Priority of Trade Liberalization

¶3. (SBU) Substantial debate had emerged in the CEPEA study group over the elements to be included in the report, according to CEPEA Study Group Chairman Risaburo Nezu. In a recent meeting with emboffs, Nezu -- a former Ministry of Economy, Trade, and Industry (METI) and OECD official and now senior managing director of the Fujitsu Economic Research Institute -- indicated the scholars from the 16 countries which would be part of CEPEA had agreed the arrangement would need to be more than just a trade pact. China and Korea argued emphasis on trade among the probable CEPEA participants would be premature. Japan's insistence on promoting trade liberalization, however, ensured the topic remained a core element of the report, Nezu said. (Note: Although the study group's formal members consisted of scholars drawn from each of the 16 countries covered by the initiative, Nezu acknowledged Japanese Foreign Ministry and METI officials were present at all meetings. The representatives of the other governments participated only occasionally. End Note.)

¶4. (SBU) As chairman, Nezu delegated the drafting of specific chapters on the report's main thematic elements to particular country representatives. Themes and assignments were: trade liberalization (Australia); trade and investment

TOKYO 00002110 002.2 OF 003

facilitation (New Zealand); economic cooperation (India); energy and environment (China); and information technology (Malaysia). Japan was charged with writing the roadmap portion containing specific policy recommendations. Chinese representative, Chinese Academy of Social Sciences researcher Zhang Yunling (who had led the previous study on a possible ASEAN Plus 3-based FTA) prepared the chapter on energy and environment because that topic was politically less controversial for China. In addition, each participant prepared an individual country paper. The country papers are not a consensus product like the full report and are designed to help participants gain a clearer understanding of each country's current preferential trade arrangements and goals they would like to achieve via CEPEA. Nezu predicted the ASEAN Economic Ministers' meeting would most likely call for no more than an additional round of study on the CEPEA proposal either on the ostensibly unofficial "Track II" basis like the current report or potentially via a more official study group composed of government officials.

¶5. (SBU) Nezu recounted disagreements over wording. For example, the South Korean participant opposed the term "open regionalism," labeling it self-contradictory. Nezu indicated he had stressed the importance of the reference to open architecture because of the political message it carried that CEPEA would not aim at creating new trade barriers and could be extended to other economies. It was particularly important to communicate this point to the United States, Nezu asserted. Nevertheless, he acknowledged while the current report lacks a section analyzing how CEPEA would interact with the U.S., EU, or APEC, it will be important to assess how it will relate with these entities should it come into being.

¶6. (SBU) Nezu also emphasized that Asia needs an institution like the OECD to act as a secretariat that facilitates, records, and disseminates research and policy discussions. Japan, he observed, has supported establishment of the Economic Research Institute for ASEAN and East Asia (ERIA) in Jakarta, Indonesia, which could serve as the basis for such an institution. (Note: ERIA also emerged from then

METI Minister Nikai's 2006 initiative. Its executive director is Hidetoshi Nishimura, a retired METI official who was previously an advisor to the Japan External Trade Organization (JETRO) and executive managing director of the Japan-China Economic Association, both organizations with close ties to METI. End note.)

METI, Industry Unwilling to Battle Opponents of Free Trade

¶7. (SBU) Waseda University Professor Shujiro Urata, one of the Japanese representatives on the CEPEA study group, noted the debate over whether the ASEAN Plus 3-based East Asia FTA (EAFTA) or the CEPEA is the optimal architecture. In a meeting with emboffs, Urata expressed concern that open acceptance among other Asian countries of CEPEA as the model for future regional architecture could damage their relations with China and even possibly South Korea, both of which support the EAFTA model. He predicts, supporters of EAFTA will come back with recommendations in 2009 to reinvigorate interest in an ASEAN Plus 3-centered architecture. Nevertheless, Urata had conducted a simulation comparing the economic benefits of CEPEA and EAFTA. He found CEPEA ultimately proved to deliver larger gains, although Urata cautioned the results depended to a great extent on the assumptions used in the model.

TOKYO 00002110 003.2 OF 003

¶8. (SBU) The Japanese bureaucracy, not business, is the driving force behind Japan's proposals for regional economic architecture, Urata observed. Japanese multinationals, he said, show little interest in supporting any particular model of regional architecture. In this regard, METI has been disappointed because Japanese business is hesitant to express its ideas. Without clear support from Japanese industry, METI is reluctant to take on the Agriculture and Health Ministries where many oppose to trade liberalization. Internationally, the GOJ also tends to let the U.S. take the lead on promoting a global trade agreement to avoid frictions with Japan's other major trading partners.

Fukao: Japan's Trade Agreements Reactive, Little Impact on Domestic Economy

¶9. (SBU) Hitotsubashi University Professor Kyoji Fukao, a participant in the study group that laid the groundwork for Japan's (stalled) economic partnership negotiations with South Korea, observed Japan has approached trade agreements primarily as a defensive measure. When Japan's trade partners look set to conclude an agreement, the GOJ begins negotiations with the relevant parties to minimize the diversionary impact on Japanese trade. The focus, he notes, is not an ambitious trade liberalization agenda. Without an institution like USTR, each GOJ ministry, Fukao stressed, can block possible concessions in any negotiation that might harm its constituency among Japanese business or the public at large.

¶10. (SBU) Fragmentation of overseas production and the current situation where exports nurture most of Japan's economic growth, signals a need for domestic reform. Fukao stressed that METI also recognizes the need to create incentives for inward investment in order to remain economically competitive. Fukao cited the example of Toyota, which he estimated has half of its total employees overseas and continues to invest most of its profits abroad, mainly to avoid paying Japanese corporate income tax. Fukao also suggested the need for Japan to diversify industries receiving FDI. Japan's service sector, for example, has yet to internationalize despite the dramatic growth in global services trade. Hence, despite language barriers, there is a great potential for globally competitive services firms to invest in Japan.

Comment

¶11. (C) Although our interlocutors -- two of them direct participants in the CEPEA study -- spoke positively about the benefits of CEPEA's "ASEAN Plus 6" architecture, none of them indicated this proposal would spur economic reform within Japan itself. Their comments tended to reinforce the perception CEPEA would serve Japan as a medium to allow it to consolidate economic relations with Asian neighbors without opening sensitive sections such as services and agriculture or diminishing its reliance on export-led growth. In addition, Nezu and Urata clearly understood the importance of references to "open regionalism" in order to mollify possible U.S. opposition to further development of CEPEA.

Nevertheless, their account of the CEPEA discussions along with Prof. Fukao's exposition of the bureaucratic dynamics involved in Tokyo lead to suspicions that any references to an open architecture in the August report will be largely rhetorical.

SCHIEFFER